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IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

HARTFORD FIRE INSURANCE CO., *et al.*,
Petitioners,
v.
STATE OF CALIFORNIA, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF OF AMERICAN INSURANCE ASSOCIATION, NATIONAL ASSOCIATION OF INDEPENDENT INSURERS, AND THE SURETY ASSOCIATION OF AMERICA AS *AMICI CURIAE* IN SUPPORT OF PETITIONERS

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TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
INTEREST OF THE *AMICI CURIAE*	1
INTRODUCTION AND SUMMARY OF ARGUMENT	3
ARGUMENT	5
I. The Decision Below Should Be Reviewed Because It Conflicts with the McCarran Act's Recognition of the Insurance Industry's Special Need for Cooperation on Policy Coverage Terms	5
II. The Lower Court's Decision Should Be Reviewed Because It Will Have a National Impact On State Regulation and Insurance Industry Practices	10
III. By Creating Substantial Uncertainty Over the Availability of McCarran Act Immunity, the Ninth Circuit's Decision Will Have the Effect, Contrary to the Statutory Purpose, of Deterring Insurers from State-Authorized Cooperation	14
A. The Decision Below Makes McCarran Act Immunity Unpredictable By Removing It Where a Plaintiff Alleges the Involvement of Non-Regulated Entities	16
B. By Defining "Boycotts" to Include All Forms of "Economic Coercion," Including Otherwise Exempt Agreements on Rates and Forms, The Lower Court's Test Would Make It Impossible to Distinguish Between Lawful and Unlawful Agreements	18
CONCLUSION	20

TABLE OF AUTHORITIES

CASES

	Page
Allied Tube & Conduit Corp. v. Indian Head, Inc., 486 U.S. 492 (1988)	15
American Soc'y of Mechanical Engrs., Inc. v. Hydrolevel Corp., 456 U.S. 556 (1982)	15
FTC v. Ticor Title Ins. Co., cert. granted, 112 S. Ct. 47 (1991)	15
Group Life & Health Ins. Co. v. Royal Drug Co., 440 U.S. 205 (1979)	5, 7
In re Workers' Compensation Ins. Antitrust Litig., 867 F.2d 1552 (8th Cir.), *cert. denied*, 492 U.S. 920 (1989)	18
National Macaroni Mfrs. Ass'n v. FTC, 345 F.2d 421 (7th Cir. 1965)	15
National Soc'y of Professional Engrs. v. United States, 435 U.S. 679 (1978)	16
St. Paul Fire & Marine Ins. Co. v. Barry, 438 U.S. 531 (1978)	4
United States v. American Radiator & Standard Sanitary Corp., 433 F.2d 174 (3d Cir. 1970), *cert. denied*, 401 U.S. 948 (1971)	15
United States v. Insurance Bd. of Cleveland, 188 F. Supp. 949 (N.D. Ohio 1960)	18
United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533 (1944)	3, 5, 6
United States v. Title Insurance Rating Bureau of Arizona, Inc., 700 F.2d 1247 (1983), *cert. denied*, 467 U.S. 1240 (1984)	15
United States v. Trenton Potteries Co., 273 U.S. 392 (1927)	15
Western & Southern Life Ins. Co. v. State Board of Equalization, 451 U.S. 648 (1981)	13

STATUTES

McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015	*passim*

MISCELLANEOUS

H.R. Rep. No. 873, 78th Cong., 1st Sess. (1943)	7, 8
R. Keeton & A. Widiss, *Insurance Law* (1988)	11

TABLE OF AUTHORITIES—Continued

	Page
Kimball & Boyce, *The Adequacy of State Insurance Regulation: The McCarran-Ferguson Act in Historical Perspective*, 56 Mich. L. Rev. 545 (1958)	11
Repeal or Revise the McCarran-Ferguson Act: Hearings Before the Senate Committee on the Judiciary, 100th Cong., 1st Sess. (1987)	5
S. Rep. No. 1112, 78th Cong., 2d Sess. (1944)	7
Tort Policy Working Group, *An Update to the Liability Crisis* (Mar. 1987)	6

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INTEREST OF THE *AMICI CURIAE*

Amici curiae are insurance trade associations and a rating organization whose members write property and casualty insurance throughout the United States.[1] The American Insurance Association ("AIA") is a national trade organization representing over 250 insurers writing property and liability coverages for businesses, homeowners, automobile drivers, and others. AIA companies together write more than $60 billion in premiums annually, representing 27 percent of all property and casualty insurance underwritten in the United States.

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[1] Petitioners and respondents have consented to the filing of this brief. Copies of the parties' consent letters have been filed with the Clerk.

The National Association of Independent Insurers ("NAII") is a national trade association representing the interests of over 560 insurers writing all varieties of property and casualty insurance. In 1990, NAII member companies wrote over $54.6 billion in direct premiums, amounting to approximately one-quarter of the total property and casualty market in the United States.

The Surety Association of America ("SAA") consists of 650 insurers that underwrite fidelity and surety bonds. SAA is licensed and regulated as either a rating or advisory organization by all the states, the District of Columbia, and Puerto Rico.

The member insurance companies of the *amici* are authorized by the laws of virtually every state to participate in state-licensed insurance rating and advisory organizations that standardize insurance policy forms such as those involved in this case. Since 1945, the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015, has afforded the *amici*'s members an antitrust exemption permitting them to comply with state regulatory policies favoring joint action without fear of federal antitrust sanctions.

The decision below, however, creates substantial uncertainty as to when that protection will continue to be available. The resulting threat of federal antitrust enforcement actions and treble damage claims will deter insurers from continuing to develop the standardized insurance coverages upon which state regulators and insurance markets now depend. In addition, the decision below will permit the federal antitrust laws to be used to challenge state-approved insurance rates and coverages —but without federal courts being able to consider, as state regulators must, the effect on insurer solvency or insurance availability.

This brief thus addresses the disruptive effect of the decision below on insurance markets and state regulatory systems. *Amici* also describe the difficulty insurers will have, under the Ninth Circuit's fact-based standard, in determining whether their compliance with state regulatory law will expose them to antitrust penalties.

INTRODUCTION AND SUMMARY OF ARGUMENT

In *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), this Court held that insurance was interstate commerce subject to the federal antitrust laws. *South-Eastern Underwriters* threatened the viability of state insurance regulation by exposing insurers to antitrust sanctions for the collective development of insurance rates and forms regarded by many states as an important part of their regulatory schemes. A year later, to resolve this uncertainty, Congress passed the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015.

Section 2(b) of the new statute, 15 U.S.C. § 1012(b), sought to prevent the federal antitrust laws from impairing existing state laws favoring industrywide cooperation, by affording insurers an antitrust exemption for state-regulated joint action. In addition, § 3(a) of the Act, 15 U.S.C. § 1013(a), imposed a three-year moratorium before the antitrust statutes would be applied to unregulated industry cooperation, thus inviting the remaining states to displace the antitrust laws by enacting laws regulating insurer collaboration. In response to Congress' invitation, forty-seven states now authorize collective ratemaking and all fifty permit standardization of policy forms.

Until the decision below, judicial interpretations of the McCarran Act afforded insurers well-defined standards for determining when their compliance with these laws would qualify for statutory immunity. Joint action on rates and forms was considered "regulated by State law," within the meaning of § 2(b) of the Act, where the state passed a statute which, on its face, subjected the rates and forms developed by licensed rating organizations to state regulatory review. Immunity for regulated rating organization activities could be lost only under the so-called "boycott" exception in § 3(b) of the Act, 15 U.S.C. § 1013(b), which this Court construed consist-

ently with the "common understanding" of a boycott as a "refusal to deal." *St. Paul Fire & Marine Ins. Co. v. Barry*, 438 U.S. 531, 532 (1978). Accordingly, prior to the decision below, there was a sharply-defined boundary between exempt and non-exempt conduct.

Cooperation between insurers in developing the *terms* of state-regulated standardized contracts, such as agreements on the scope of coverage, were immune because they did not constitute a "refusal to deal"—they merely established the contractual terms upon which a deal would be made. These cooperative agreements on the coverage terms of insurance policies were distinguished from refusals to sell policies on *any* terms. Such outright refusals to deal were the essence of a group boycott and were not part of the state-regulated cooperation on coverage terms that Congress wished to protect.

The decision below abandons these bright line distinctions. The court of appeals has instead substituted inherently unpredictable inquiries depriving insurers of advance assurance that their state-authorized collaboration will not expose them to antitrust sanctions. Even where, as here, state regulators actively reviewed and explicitly approved the terms of standardized policies as being fair to policyholders, the decision below would permit use of the Sherman Act to overturn those regulatory decisions based on assertions that coverage terms were "economically coercive" or were influenced by "non-exempt" out-of-state parties. The lower court's decision will also permit antitrust plaintiffs to challenge state-approved insurance rates under the same rationale.

The decision below thus places in jeopardy as a "boycott" every agreement among insurers that establishes the coverages or price of an insurance contract. This result is fundamentally in conflict with the purpose of the McCarran Act's antitrust exemption, which was to protect state-authorized cooperation on rates and forms, and will place insurers in the untenable position of complying with conflicting state regulatory and federal antitrust standards.

ARGUMENT

I. The Decision Below Should Be Reviewed Because It Conflicts with the McCarran Act's Recognition of the Insurance Industry's Special Need for Cooperation on Policy Coverage Terms

The McCarran Act was Congress' response to the Justice Department's effort in the early 1940s to prohibit collective ratemaking by state-licensed rating bureaus. *See Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 217 (1979). The Act overruled *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944), in which the Court sustained, on interstate commerce grounds, a Sherman Act indictment against 200 fire insurance companies in six states that established rates through fire inspection and rating bureaus.

The present cases are a renewed attempt to apply the Sherman Act to prohibit rating organization activities—in this instance, the standardization of policy forms and ratemaking support for those forms. The lead plaintiffs, the attorneys general of nineteen states, contend that the defendants agreed to restrict the coverage terms of commercial liability insurance policies, thereby causing the so-called "crisis" in the availability of this insurance during the early and mid-1980s. Both the Justice Department and the Federal Trade Commission have investigated and rejected this thesis.[2] In addition, virtually

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[2] *See Repeal or Revise the McCarran-Ferguson Act: Hearings Before the Senate Committee on the Judiciary*, 100th Cong., 1st Sess. 53-54 (1987) (statement of Charles F. Rule, Acting Assistant Attorney General, Antitrust Division) ("Hence it seems highly probable that the property/casualty industry is in fact competitive, and that collusion is not responsible for the availability and affordability crisis in certain lines of insurance."); Letter from Douglas H. Ginsburg, Assistant Attorney General, Antitrust Division, United States Department of Justice, to Jay Angoff, National Insurance Consumer Organization (Apr. 22, 1986) ("The Federal Trade Commission has within the last six months investigated similar charges concerning the pricing and availability of certain lines of property and casualty insurance . . . I understand that the Commission

every state approved the challenged forms as proposed by defendants or after modifications required by regulators; the forms could not be used in the few jurisdictions disapproving them. Pet. App. 38a.

Plaintiffs nevertheless seek treble damages amounting to a substantial reduction in the rate levels previously approved by state regulators. They also seek injunctive relief revising the terms of the insurance policies previously approved by the states; limiting the industry's ability to standardize policy forms; and altering the governance of the Insurance Services Office, the largest state-regulated rating organization.

The decision below is thus important to the insurance industry for the same reason that *South-Eastern Underwriters* was. By exposing insurers to federal antitrust sanctions for state-authorized cooperation, the Ninth Circuit's rulings threaten significant deregulation and restructuring of the property and casualty industry. The crucial difference between the present cases and *South-Eastern Underwriters*, however, is that Congress has made an intervening policy decision that the Sherman Act should not apply to joint action on rates and policy forms where regulated by the states.

Congress' judgment was based on its conclusion that industry cooperation, not competition, maximizes the availability and affordability of insurance. Both Senate and House members regarded insurance as "something quite different from the ordinary commercial transaction" and believed that the distinctive nature of the product

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has now closed the investigation because it was unable to find any evidence of collusion."); "The Crisis in Property-Casualty Insurance", Antitrust Division, United States Department of Justice, Appendix to *An Update on the Liability Crisis*, Tort Policy Working Group (Mar. 1987) ("It has been asserted that a principal cause of the crisis has been concerted, anticompetitive actions by insurers to raise prices in certain lines of property-casualty insurance or even to refuse to write such insurance. Economic analysis of the relevant insurance markets, however, leads to the conclusion that such a scenario is implausible.").

demanded "[u]niformity as to rates, forms of policies and the like." H.R. Rep. No. 873, 78th Cong., 1st Sess. 8 (1943); *see also* S. Rep. No. 1112, 78th Cong., 2d Sess. 6 (1944). The McCarran Act's antitrust exemption was enacted because such "[u]niformity as to rates, forms of policies, terms, and conditions . . . is only possible as a result of joint action and cooperation." 90 Cong. Rec. 6536 (1944) (statement of Rep. Howell).

In affording antitrust immunity for standardization of insurance policies, proponents of the McCarran Act expressed three distinct reasons why uniformity and industry cooperation was in the public interest. First, Congress was persuaded by state officials that standard coverage terms were an integral part of the industry cooperation on rates which the regulators regarded as essential.

Unlike virtually all other products, insurance must be priced before its most significant costs are known—the future losses against which the insurer indemnifies the policyholder. The authors of the McCarran Act thus recognized that "[t]hese factors are not within the control of insuring companies in the sense that the producer or manufacturer may control cost factors." H.R. Rep. No. 873, 78th Cong., 1st Sess. 8-9 (1943), *quoted in Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. at 221.

Efficient pricing of insurance accordingly requires accurate prediction of future losses which, in turn, requires industrywide pooling of historical loss data and centralization of actuarial expertise. Congress correspondingly agreed with state regulators that "concert of action in the collection of statistical data and ratemaking" was a "necessity" which would make it "a mistake to permit or require the unrestricted competition contemplated by the antitrust laws." 440 U.S. at 221-22 (quoting report of the National Association of Insurance Commissioners submitted to Congress Nov. 16, 1944).

Congress further recognized that cooperation on rates was not possible unless insurers also could standardize their coverages. State regulators had convinced Congress that statistical information on losses could not meaningfully be pooled and analyzed unless the data related to standard definitions of risk. *See, e.g.*, H.R. Rep. No. 873, 78th Cong., 1st Sess. 9 (1943) (the "distribution of risks . . . in their bearing upon rates and forms of policy can best be determined through cooperative action"). The decision below will frustrate this congressional objective by permitting antitrust plaintiffs to obtain injunctive relief mandating diversity in insurance forms rather than uniformity.

Reinsurance was the second reason why the McCarran Act exempted standardization of coverage terms. Congress considered reinsurance as vital to the underwriting of potentially catastrophic risks that no insurer prudently could underwrite on its own. The legislators were concerned that the absence of standardized coverages might pose a substantial barrier to obtaining reinsurance: "No company could safely agree in advance to reinsure, unless it knew what the terms of its obligations would be and the consideration therefor." H.R. Rep. No. 873, 78th Cong., 1st Sess. 9 (1943); *see also* 90 Cong. Rec. 6527 (1944) (statement of Rep. Miller) (if "companies are not going to be permitted to get together and agree on rates, forms, and the establishment of rating bureaus . . . [h]ow could there be reinsurance? . . . If we did not have uniform rates and forms, how could such reinsurance be placed?"); *id.* at 6528 (statement of Rep. Miller) (without standard rates, "each reinsurance transaction will involve negotiations between the insurer and all of its reinsurers, and this will involve such delay and expense as to make impossible the expeditious insurance of large risks"). By threatening insurers and reinsurers with antitrust sanctions for cooperating on standardized coverages, the decision below will impede insurer access to reinsurance in precisely the manner Congress sought to avoid.

The third reason for immunizing industry cooperation on coverage terms was to preserve state consumer protection laws mandating or encouraging standardized policies. Most states had adopted laws of this type prior to the McCarran Act. *See* 90 Cong. Rec. 6538 (1944) (statement of Rep. Springer) ("Laws have been enacted by the States to control the insurance business . . . the people have been fully protected by having reasonable rates and we have uniform contracts which fully protect the insured."); *id.* at 6556 (statement of Rep. Graham) ("The States have established uniform fire-insurance policies, so that today 31 States prescribe standard forms of policies that must be used.").

The McCarran Act was intended to prevent the antitrust laws from impairing these laws by prohibiting the industry cooperation necessary to their success: "A State law relating to regulation, for instance, . . . the fixing of the terms of a contract of insurance, which might under some definitions of monopoly be monopolistic, would be permitted under the pending bill." 91 Cong. Rec. 480-81 (1945) (statement of Sen. Ferguson). The decision below, by permitting antitrust plaintiffs to override state authorization and approval of standardized forms, would thus undermine a category of state laws that Congress specifically sought to protect.

More generally, an important objective of the McCarran Act was to preserve state laws authorizing and regulating rating organizations, since these were the mechanisms through which the states implemented policies favoring uniform coverage terms and standard rates. Senator Ferguson, one of the principal sponsors of the new legislation, emphasized that "certain things are essential, at least in the opinion of many of the States, and one is a rating bureau." 90 Cong. Rec. 6627 (1944).

To accommodate the states, Senator Ferguson said his bill "would permit—and I think it is fair to say that it is intended to permit—rating bureaus . . . What we saw as wrong was the fixing of rates without statutory au-

thority in the States; but we believe that State rights should permit a State to say that it believes in a rating bureau." 91 Cong. Rec. 1481 (1945). Accordingly, the main purpose of the antitrust exemption in § 2(b) of the Act was to preclude the federal antitrust laws from conflicting with state authorization of rating organizations and the states' exercise of exclusive regulatory jurisdiction over them.

The decision below is fundamentally at odds with this congressional recognition that cooperative actions essential to the unique nature of insurance be regulated by the states. The Ninth Circuit opinion will contravene this clearly expressed intent because parties dissatisfied with state regulation will now be able to use the Sherman Act as a federal regulatory tool for obtaining restrictions on the operations and governance of rating organizations irrespective of whether those limitations are consistent with state regulatory policy. Indeed, the decision below will adversely affect the regulatory systems of all fifty states and have nationwide repercussions for insurance markets dependent on standardized forms.

II. The Lower Court's Decision Should Be Reviewed Because It Will Have a National Impact On State Regulation and Insurance Industry Practices

The Ninth Circuit ruled that the federal antitrust laws could be applied to standardization of insurance policy forms where the states, although they review and approve or reject the policy forms proposed by insurers, do not additionally limit participation in the forms development process to "exempt" entities. Pet. App. 20a. None of the fifty states, however, regulate forms in the manner required by the Ninth Circuit.

As noted in Part I, *supra*, one purpose of the McCarran Act's antitrust exemption was to prevent federal impairment of widespread state laws requiring or authorizing standardization of fire insurance policies. Congress obviously intended, therefore, that regulation of this variety should satisfy the state regulation requirement

for affording antitrust immunity. Indeed, Congress encouraged the states to enact similar laws by imposing a three-year moratorium on application of the antitrust laws so that the states would have time to act before the federal statutes could be invoked to end this industry collaboration. *See* 15 U.S.C. § 1013(a).

Almost all of the states that had not enacted laws regulating rates and forms before 1945 accepted Congress' invitation. By 1951, virtually every state had adopted laws which licensed insurance rating and advisory organizations, authorized them to develop standard rates and forms, and afforded insurance department reviewing authority over the rates and forms proposed by these industry associations.[3]

Today, no less so than during the period immediately after passage of the McCarran Act, the states consider standardization of coverage terms by rating organizations as an important feature of their regulatory policy. All fifty states, the District of Columbia, and Puerto Rico, with only partial exceptions in eight jurisdictions, authorize insurers to jointly develop forms for property and casualty insurance, fidelity bonds, and workers compensation and employers' liability coverage. In recognition of the close linkage between forms and rates, forty-seven states, the District of Columbia, and Puerto Rico similarly authorize insurers to formulate joint rates or engage in other forms of rate-related cooperation.

None of these states restrict participation in the forms development process solely to insurers licensed with the particular state or to other parties directly and independently subject to the insurance department's regulatory jurisdiction. For example, a state will often consider nationally standardized forms proposed by national rating

[3] *See* Kimball & Boyce, *The Adequacy of State Insurance Regulation: The McCarran-Ferguson Act in Historical Perspective*, 56 Mich. L. Rev. 545, 555 (1958); R. Keeton & A. Widiss, *Insurance Law*, § 8.4, at 959-60 (1988).

organizations, reflecting the views of insurers which may not transact business in the reviewing jurisdiction. If they refused to review such forms because of the involvement of a "non-exempt" entity, the states could not exercise their regulatory power over important insurance coverages. Similarly, the states often consider forms reflecting the input of unregulated parties, since a refusal to do so would prevent reinsurers, insurance purchasers, and other interested persons from expressing their views on forms being considered by insurance rating organizations.

The Ninth Circuit's standard for affording McCarran Act immunity, however, requires that the state have direct regulatory authority—independent of the states' power to review form filings—over all parties that influenced those filings. The lower court's ruling would thus compel the states to choose between: (1) excluding anyone but locally-licensed insurers from the form standardization process; or (2) exposing insurer members of rating organizations to possible antitrust sanctions if the states continued to allow broader access.

Indeed, by conditioning McCarran Act immunity on the noninvolvement of out-of-state entities, the decision below would impose a dual federal-state regulatory regime in most insurance markets. Virtually all lines of insurance are interstate or international in character. Consequently, there will always be some element of commerce in these markets not occurring within a particular state's boundaries. The lower court's standard, however, would remove McCarran immunity for the conduct of all state-regulated insurers based on the alleged involvement of a single unregulated party. It thus would permit application of the Sherman Act not just to out-of-state conduct beyond a state's jurisdiction because of its purely extraterritorial effects but also to conduct clearly within the scope of a state's jurisdiction, such as in-state conduct and out-of-state conduct having substantial local effects.

The lower court's refusal to apply the McCarran exemption to conduct manifestly within the scope of state regulatory jurisdiction would permit antitrust plaintiffs to seek injunctive and monetary relief inconsistent with state regulatory decisions, such as the substantial modifications sought by the present plaintiffs in the terms of insurance policies previously approved by state regulators. This application of the Sherman Act to regulate insurance market practices cannot be squared with Congress' intention, expressed through the McCarran Act, to delegate exclusively to the states its broad Commerce Clause power to regulate insurance. *See Western & Southern Life Ins. Co. v. State Board of Equalization*, 451 U.S. 648, 653 (1981).

The withholding of McCarran Act immunity under the Ninth Circuit's rationale will have disruptive consequences for insurance markets as well as for state regulation. In most lines of insurance, both insurers and policyholders substantially depend on standardized coverages. As the McCarran Act's legislative history repeatedly recognizes, insurers need uniform coverage terms in order to accurately price their product and to obtain reinsurance maximizing their underwriting capacity. In addition, judicial interpretation of standard contract terms creates a body of law upon which insurers and insureds can rely. Standardized coverages also benefit policyholders by allowing them to more readily compare the products of competing insurers on the basis of price or quality of claims service.

The Ninth Circuit's decision threatens to deny insurers and insureds these benefits of form standardization. Antitrust plaintiffs, like those in the present action, could seek injunctive relief compelling rating organizations to develop multiple, non-uniform coverages or to make abrupt changes in policy terms upsetting settled contractual expectations.[4] Since coverage terms in many

[4] *See, e.g.*, Complaint of State of California ¶¶ 163, 164 (request for injunction to modify terms of existing standard policies and compel reinstitution of superseded coverages).

lines of insurance are nationally standardized or developed by nationally-operating rating organizations, actions brought in the Ninth Circuit could affect coverage terms throughout the country.

Application of the Sherman Act to state-approved coverage terms and rates also could have an adverse effect on the financial condition of insurers. To maintain insurer solvency, virtually all states require that insurance rates not be "inadequate" for the risks being assumed. The federal antitrust laws, however, express a policy of unrestrained competition even if the result is bankruptcy. Unlike state regulators, therefore, federal courts would not be empowered, let alone have the expertise, to determine whether expanded coverage terms or rate reductions sought by antitrust plaintiffs might impair the ability of insurers to pay future claims.

The danger posed by the decision below, therefore, is precisely what the McCarran Act was intended to avert: imposition on the states and the insurance industry of a one-dimensional procompetition policy preventing application of regulatory standards designed to accommodate other important public policies.

III. By Creating Substantial Uncertainty Over the Availability of McCarran Act Immunity, the Ninth Circuit's Decision Will Have the Effect, Contrary To the Statutory Purpose, of Deterring Insurers from State-Authorized Cooperation

The Ninth Circuit's decision will most significantly affect insurers by creating substantial uncertainty over their exposure to antitrust sanctions for engaging in state-authorized cooperation. The decision below abandons the bright line standards adopted in prior McCarran Act jurisprudence in favor of complex jurisdictional and market tests that leave insurers unable to determine, in advance and with reasonable certainty, whether their conduct will qualify for antitrust immunity. In addition, in the event that antitrust actions are brought against insurance rating organizations and their members, the

Ninth Circuit's fact-based analysis will make it difficult to obtain dismissal on the pleadings or summary judgment, further heightening uncertainty over the availability of the McCarran exemption. Prudent insurers will regard this ambiguity as a powerful deterrent to continuing participation in rating organization activities, since collective ratemaking and form standardization would present serious antitrust risks absent immunity.

Both the Justice Department and Federal Trade Commission take the position that cooperation by insurers on rates is *per se* illegal absent McCarran Act immunity. *See, e.g., FTC v. Ticor Title Ins. Co., cert. granted*, 112 S. Ct. 47 (1991); *United States v. Title Insurance Rating Bureau of Arizona, Inc.*, 700 F.2d 1247 (1983), *cert. denied*, 476 U.S. 1240 (1984). Under the *per se* rule, insurer agreements on prices would be conclusively presumed unlawful irrespective of whether the rates were reasonable and without regard to the insurance industry's unique need for cooperation on rates. *United States v. Trenton Potteries Co.*, 273 U.S. 392 (1927).

Form standardization would present similar antitrust risks absent McCarran immunity. Standards-setting organizations and their members are subject to intensive antitrust scrutiny, especially where product standards significantly affect pricing. *See Allied Tube & Conduit Corp. v. Indian Head, Inc.*, 486 U.S. 492, 500 (1988); *American Soc'y of Mechanical Engrs., Inc. v. Hydrolevel Corp.*, 456 U.S. 556 (1982); *United States v. American Radiator & Standard Sanitary Corp.*, 433 F.2d 174 (3d Cir. 1970), *cert. denied*, 401 U.S. 948 (1971); *National Macaroni Mfrs. Ass'n v. FTC*, 345 F.2d 421 (7th Cir. 1965). Even though standardization of insurance coverages might not be *per se* illegal, but instead subject to the less stringent "rule of reason," the antitrust laws still might not permit a defense based on the insurance industry's unique need to avoid proliferation of coverage terms. Under the "rule of reason," the inquiry is limited to whether the challenged practice "is one that promotes

competition or one that suppresses competition." *National Soc'y of Professional Engrs. v. United States*, 435 U.S. 679, 691 (1978). Because the inquiry is thus "confined to a consideration of impact on competitive conditions," the "rule of reason" does not permit a defense "based on the assumption that competition itself is unreasonable" or based on a market's special needs. *Id.* at 696.

The McCarran Act's antitrust exemption sought to resolve this basic tension between the federal antitrust laws and state laws recognizing the insurance market's unique characteristics. The decision below, however, will return insurers to the era of regulatory uncertainty predating the McCarran Act. Insurers no longer will have well-defined standards for determining when they are sufficiently "regulated by State law" so as to qualify for McCarran immunity; they similarly will lack well-articulated criteria for determining when their conduct amounts to a non-exempt "boycott" rather than an exempt agreement on rates or forms.

A. *The Decision Below Makes McCarran Act Immunity Unpredictable By Removing It Where a Plaintiff Alleges the Involvement of Non-Regulated Entities*

The insurance policy forms challenged by the plaintiffs were regulated in all of the relevant states by laws authorizing state regulators to review them for fairness to policyholders. Pet. App. 48a-49a. The court below nevertheless denied immunity to the domestic insurer and reinsurer defendants based on plaintiffs' allegation that they solicited the assistance of foreign-based reinsurers, not subject to the states' jurisdiction, to influence the contents of the forms prior to being proposed to state regulators. *Id.* at 20a. In effect, the lower court engrafted a new "non-exempt entity" exception onto the McCarran exemption permitting application of the federal antitrust laws to regulated insurers whenever a plaintiff alleges that an out-of-state or unregulated party influenced their development of a standard rate or form.

For insurers planning their business operations and compliance with state regulatory requirements, this "non-exempt entity" exception eliminates predictability in determining when collective action on rates or forms will be free from antitrust sanction. Insurers formerly could assess the availability of immunity merely by examining relevant provisions of a state's insurance code to determine if collective forms development or collective ratemaking was authorized and the forms or rates regulated. Now, insurers must reckon with the possibility that statutory authorization will not be enough if, years after their collaboration, an antitrust plaintiff alleges an agreement with a "non-exempt" entity.

The decision below also places insurers in the dilemma of losing their McCarran Act immunity whether or not they deal with "non-exempt" parties. Numerous unregulated or out-of-state, and hence "non-exempt," parties frequently express their views on, or otherwise influence, the proposed forms and rates being considered by insurance rating organizations. Interested parties include professional actuarial societies, insurer trade associations, purchasers of insurance coverage (*e.g.*, corporate risk managers), consumer organizations, insurance agents and brokers, and reinsurers. In addition, many of the members of national rating organizations do not sell insurance in all fifty states and thus would be "non-exempt" entities where rating organization activities in one of those states are challenged.

If insurers permit these "non-exempt" entities to participate in the form standardization or collective ratemaking process, they risk not qualifying for immunity under the McCarran Act's state regulation requirement if an antitrust plaintiff alleges, years after the fact, that there was collusion with those parties. Indeed, under the Ninth Circuit's approach, immunity would be stripped away even if a plaintiff did not allege that the agreement between the regulated insurers and the unregulated parties amounted to a "boycott" within the meaning of the Act. Rather, the effect of the involvement of an

unregulated entity is that the entire cooperative enterprise is held not to be "regulated by State law," even if the states thoroughly regulate rating organizations and the forms and rates they develop. Conversely, if regulated insurers seek to protect themselves against this antitrust exposure, by refusing to permit participation by "non-exempt" entities in the standards-setting process, they run the risk of losing immunity under the McCarran Act's "boycott" exception.[5]

B. *By Defining "Boycotts" to Include All Forms of "Economic Coercion," Including Otherwise Exempt Agreements on Rates and Forms, The Lower Court's Test Would Make It Impossible to Distinguish Between Lawful and Unlawful Agreements*

The decision below will additionally deter insurers from engaging in state-authorized cooperation because it provides no meaningful criteria for predicting whether joint action on rates and forms will be considered an agreement exempt under § 2(b) of the McCarran Act or a boycott losing the exemption under § 3(b).

The "boycotts" alleged in plaintiffs' complaints were agreements by the defendants refusing or threatening not to sell reinsurance on the terms desired by plaintiffs, but only on other terms favored by the defendants, so as to "coerce" insurers to use similar terms in their coverages. On its face, therefore, the alleged conduct, whether characterized as an agreement on uniform primary insurance terms or on uniform reinsurance terms, ordinarily would have immunity under § 2(b) of the McCarran Act.

The lower court nevertheless considered these agreements to be boycotts because of their allegedly coercive purpose, defendants' "economic power," and the corresponding compulsion on buyers to agree to the defendants' terms involuntarily. Pet. App. 24a. This ruling was based on the appellate court's broad definition of "boycott" as any "use of economic power of a third party to force the boycott victim to agree to the boycott beneficiary's terms." *Id.* at 23a. Under the lower court's "economic coercion" test, therefore, the "boycott" exception would be applied based on an inquiry into the defendants' intent, the extent of their market power, and the economic impact on the purchasers of insurance or reinsurance.

This standard offers no principled basis for distinguishing between boycotts and exempt agreements on rates and coverage terms. All agreements by a rating organization's members on uniform rates and terms might exercise "economic coercion" on policyholders in the Ninth Circuit's sense that the insurers intended to influence purchasing decisions, had market power, and deprived insureds of other options. Consequently, all cooperation on rates and forms potentially could lose immunity under the boycott exception.

The availability of immunity in a particular case would depend on the uncertain outcome of a fact-based analysis akin to the "rule of reason" standard employed in Sherman Act cases. The factfinder would have to examine the intentions of the cooperating insurers, to determine whether their agreement was designed merely to set uniform rates and terms or instead was intended to achieve some ulterior "coercive" purpose. A similar inquiry would be required into the impact of the agreement on buyers' options in the market and their perceptions, to see if they voluntarily agreed to the challenged coverage terms or acquiesced in them only because "coerced."[6]

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[5] *See, e.g., In re Workers' Compensation Ins. Antitrust Litig.*, 867 F.2d 1552 (8th Cir.), *cert. denied*, 492 U.S. 920 (1989) (threatened exclusion of insurers from a rating organization); *United States v. Insurance Bd. of Cleveland*, 188 F. Supp. 949 (N.D. Ohio 1960) (exclusion of insurance agents from trade association).

[6] Ironically, the conduct alleged in the complaint should not have qualified as "coercive" under the Ninth Circuit's own test. The plaintiffs alleged four "coercive" restrictions in coverage terms, none of which actually deprived policyholders of any purchasing option. For example, the plaintiffs' principal grievance was that defendants sought to eliminate "occurrence"-based coverage in favor of more restrictive "claims-made" coverage. In fact, both types of coverage

Indeed, the Ninth Circuit's standard for applying the "boycott" exception could render the McCarran exemption substantially meaningless. The whole purpose of affording antitrust immunity to state-regulated agreements on rates and forms was to avoid the analysis of their competitive purpose and effects which would be required under the antitrust laws. Yet the lower court's standard is based on precisely these factors and would afford immunity only for "noncoercive" conduct which probably would not violate the antitrust laws in any event.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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were available in the market and more than 95 percent of purchasers exercised their option of buying the broader type of policy.